

Message Text

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C O N F I D E N T I A L PARIS 13924

E. O. 11652: GDS

TAGS: EFIN, FR, US

SUBJECT: NIXON- POMPIDOU SUMMIT: AGENDA ITEM II A - INTERNATIONAL
MONETARY REFORM

REF: PARIS 11891 AND 11892

1. AS PROMISED REFTEL, FOLLOWING IS FURTHER DISCUSSION OF AGENDA ITEM ON INTERNATIONAL MONETARY REFORM. IT STRESSES ISSUES WHICH WILL BE UPPERMOST IN MIND OF PRESIDENT POMPIDOU, PARTICULARLY POINTS WHERE FRENCH AND U. S. APPROACHES DIFFER WIDELY.
2. CONVERTIBILITY. POMPIDOU WILL PROBABLY BEAR DOWN HARDEST ON IMPORTANCE OF AGREEING AT EARLIEST POSSIBLE MOMENT ON CONDITIONS FOR RESUMPTION OF GENERAL CURRENCY CONVERTIBILITY, AND MORE PARTICULARLY OF DOLLAR CONVERTIBILITY. (SEE, FOR EXAMPLE, PARIS 13534.) IN FRENCH VIEW, CONVERTIBILITY ARRANGEMENTS SHOULD BE DESIGNED SO THAT SETTLEMENTS OF BALANCES BETWEEN CENTRAL BANKS ARE MADE ONLY IN RESERVE ASSETS THAT CANNOT BE CREATED AT WILL BY A SINGLE NATION. IN CONNECTION WITH RESTORATION CONVERTIBILITY, GOF IS READY EXAMINE METHODS OF CONSOLIDATING EXISTING DOLLAR BALANCES. IN DISCUSSING THIS ISSUE, WE COULD AGAIN EMPHASIZE: A) LINK BETWEEN CONVERTIBILITY ARRANGEMENTS AND OTHER ELEMENTS OF REFORMED SYSTEM, AND B) GREAT DIFFICULTY OF RESTORING DOLLAR CONVERTIBILITY BEFORE WE REACH BALANCE OF PAYMENTS EQUILIBRIUM.
3. GOLD AND RESERVE ASSETS. GOF HAS COME SOME DISTANCE IN
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ENDORING CONCEPT THAT SDR WILL BE MAJOR INSTRUMENT FOR ASSURING FUTURE RESERVE GROWTH. THEY STILL STRONGLY BELIEVE, HOWEVER, PRACTICALLY AS AN ARTICLE OF FAITH, THAT GOLD SHOULD CONTINUE AS ONE OF THE LINCHPINS OF THE SYSTEM. POMPIDOU WILL EXPRESS GRAVE DOUBTS THAT SDRS CAN SUCCESSFULLY REPLACE GOLD AS ULTIMATE RESERVE ASSET. OUR REBUTTAL COULD EFFECTIVELY STRESS RECENT EVENTS. VOLATILE BEHAVIOR OF FREE GOLD MARKET, WHICH IS VERY THIN AND DEPENDENT ON SOUTH AFRICAN AND RUSSIAN SUPPLY, CLEARLY ILLUSTRATES PROBLEMS IN RETAINING IMPORTANT TRADE COMMODITY AS ULTIMATE MONETARY STANDARD.

4. CAPITAL CONTROLS. FRENCH BUREAUCRATIC TRADITIONS HAVE CONDITIONED GOF TO IMPORTANCE USE CAPITAL CONTROLS AS DEVICE FOR DEALING WITH DISEQUILIBRATING MONEY FLOWS. AS THEY SEE IT, IN WORLD WHERE MASSIVE AMOUNTS OF MONEY CAN MOVE SUDDENLY IN RESPONSE TO SPECULATIVE PRESSURES, COUNTRIES MUST HAVE WAYS OF PREVENTING THEMSELVES FROM BEING DROWNED IN OR DRAINED OF LIQUIDITY. OUR APPROACH TO CONTROLS STRENGTHENS GOF FEELING THAT WE SEEK A STRONG TRADE ACCOUNT IN ORDER FINANCE CONTINUED STREAM OF OUTWARD DIRECT INVESTMENT TO INDUSTRIALIZED NATIONS. IN DEALING WITH THESE POINTS, WE COULD CONCEDE THAT SOME COUNTRIES MAY HAVE TO EMPLOY CAPITAL CONTROLS TEMPORARILY ON SOME OCCASIONS. IN GENERAL, HOWEVER, WE SHOULD CONTINUE EXPRESS STRONG VIEW THAT COST OF CONTROLS IN DISTORTING ALLOCATION OF WORLD RESOURCES IS TOO HIGH TO PAY.

5. THE ADJUSTMENT PROCESS. GOF, DESPITE FACT IT NOW IS PARTICIPATING IN JOINT FLOAT, PREFERS SYSTEM WITH CONSIDERABLY LESS FLEXIBILITY THAN WE WOULD LIKE TO SEE. FOR FRANCE, PARITIES SHOULD BE MORE " STABLE" OR " FIXED" THAN " ADJUSTABLE". POMPIDOU CAN BE EXPECTED TO EMPHASIZE IMPORTANCE OF CLASSIC TOOLS OF MONETARY AND FISCAL POLICY AS ALTERNATIVE TO FLOATING IN RESTORATION EXTERNAL EQUILIBRIUM. HE WILL ALSO BE SUSPICIOUS OF ANY USE OF AUTOMATIC (AS OPPOSED TO INDICATIVE) INDICATORS TRIGGERING EXCHANGE RATE ADJUSTMENT. IN COUNTERING SUCH ARGUMENTS, WE COULD POINT TO A) INSTABILITY INTRODUCED INTO BRETON WOODS SYSTEM BY STICKINESS OF EXCHANGE RATES, AND B) DIFFICULTY FOR COUNTRIES OPERATING IN CURRENT ECONOMIC ENVIRONMENT TO GIVE EXTERNAL OBJECTIVES PRIORITY OVER DOMESTIC ONES.

6. TIMING OF NEGOTIATIONS. GOF HAS TAKEN PUBLIC POSITION THAT NEGOTIATIONS TOWARD REFORM ARE MOVING TOO SLOWLY, LARGELY BECAUSE

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SHORT- TERM CRISES CREATED BY PERSISTENT U. S. BALANCE OF PAYMENTS DEFICIT DIVERT ATTENTION OF GOVERNMENTS AWAY FROM LONG- TERM PROBLEMS. POMPIDOU WILL BE PESSIMISTIC ABOUT POSSIBILITY OF REACHING AGREEMENT, EVEN ON GENERAL PRINCIPLES, BY FALL OF

1973. ECHOING THEME SOUNDED BY FINANCE MINISTER GISCARD D'ESTAING AT IMF MEETING LAST FALL, HE MAY SUGGEST CONCENTRATING FIRST ON ONE OR TWO SPECIFIC AREAS - E. G. EXCHANGE RATE MECHANISMS AND MONETARY ARRANGEMENTS IN FAVOR DEVELOPING NATIONS. THIS WOULD SIGNAL FRENCH TACTIC OF WEARING DOWN OTHER NEGOTIATORS TO ELICIT CONCESSIONS IN DIRECTION FRENCH VIEWPOINTS ON QUESTIONS SUCH AS ROLE OF GOLD WHERE FRENCH ARE VERY MUCH ISOLATED. HERE, WE COULD USEFULLY ELABORATE OUR CONCEPT THAT MONETARY REFORM CANNOT BE ACCOMPLISHED PIECEMEAL SINCE ALL ELEMENTS OF SYSTEM STRONGLY INTERACT.

7. UNLIKE SITUATION AT TIME AZORES MEETING, OUTSTANDING MONETARY ISSUES DO NOT SEEM RIPE FOR SETTLEMENT IN ICELAND. CONSEQUENTLY, WE BELIEVE BEST U. S. TACTIC WOULD BE AVOIDANCE DETAILED DISCUSSION OF TECHNICAL POINTS ON GROUNDS C-20 IS BEST PLACE TO RESOLVE THEM. OUR OBJECTIVE SHOULD RATHER BE A JOINT STATEMENT EXPRESSING URGENCY OF PROGRESS IN C-20 AND IMPORTANCE ACHIEVING SUBSTANTIAL AGREEMENT ON OUTLINE OF REFORM PLAN IN TIME FOR NAIROBI MEETING. IF WE WISHED TO OBTAIN FRENCH AGREEMENT AT THIS MEETING ON SUCH QUESTIONS AS FLEXIBILITY, THE ADJUSTMENT PROCESS, CAPITAL CONTROLS, ETC., WE BELIEVE WE WOULD HAVE TO PAY A PRICE IN THE FORM OF CONCESSIONS ON CONVERTIBILITY AND THE ROLE OF GOLD WHICH WE ASSUME WE ARE NOT PREPARED TO PAY. IRWIN

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